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No. 82-435

IN THE

Supreme Court of the United States

October Term, 1982

COMMONWEALTH EDISON COMPANY, *ET AL.*,
Petitioners,

v.

UNITED STATES OF AMERICA and
INTERSTATE COMMERCE COMMISSION,
Et Al., Respondents.

ON WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE
DISTRICT OF COLUMBIA CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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September, 1982

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QUESTIONS PRESENTED

1. Where a statute directs the Interstate Commerce Commission to determine the increase in railroad costs on a quarterly basis and authorizes the railroads to increase rates by the amount so determined, and the Commission adopted a procedure that it knew would result in authorized increases in excess of the increases in railroad costs, did the Court below have a duty to set aside the Commission decision?

2. Where the Interstate Commerce Commission adopted the Association of American Railroads Index of Railroad Material Prices and Wages as the measure of increases in cost, and declined, as a matter of policy, to adjust that index for changes in productivity although it conceded that it could make such an adjustment, and the Court below found that the alleged policy reasons were invalid, did the Court err in sustaining the Commission based on the Court's view as to the difficulties involved in making a productivity adjustment?

LIST OF PARTIES

This Petition is being filed on behalf of the following: Commonwealth Edison Company;[1] Madison Gas and Electric Company;[2] Pennsylvania Power & Light Company;[3] Wisconsin Power & Light Company;[4] and Wisconsin Public Service Corporation[5].

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[1]*Subsidiaries and Affiliates:* Chicago & Illinois Midland Railway Company; Commonwealth Edison Company of Indiana, Inc.; Commonwealth Research Corporation; Concomber, Inc.; Cotter Corporation; Edison Development Company; Edison Development Company Canada, Inc.; Medical Center Steam Company; and 72 West Adams Company.

[2]*Subsidiaries & Affiliates:* Madison Gas & Electric Foundation, Inc., Madison Gas & Electric; Nuclear Fuel, Inc.; Magael, Inc.; and Magael Material Resources, Inc.

[3]*Susidiaries & Affiliates:* The Arcadia Company, Inc.; BDW Corporation; Court Development Company; Greene Hill Coal Company; Greene Manor Coal Company; Hanover Development Company; Interstate Energy Company; LCA Leasing Corporation; The Oneida Mining Company; Pemico, Inc.; Pennsylvania Mines Corporation; Realty Company of Pennsylvania; Rushton Mining Company; Service Development Company; Tunnelton Mining Company; and Uranium Resources and Development Company.

[4]*Subsidiaries & Affiliates:* Nufus, Inc.; South Beloit Water, Gas & Electric Company; Wisconsin Power & Light; Nuclear Fuel, Inc.; and Wisconsin River Power Company.

[5]*Subsidiaries & Affiliates:* Dolors Bench General Partners.

The following were also parties to the proceeding in the United States Court of Appeals for the District of Columbia Circuit:

Alabama Power Company
American Iron & Steel Institute
American Paper Institute
Arkansas Power & Light Company
Association of American Railroads
Carolina Power & Light Company
Central Illinois Light Company
Chemical Manufacturer's Association
Duke Power Company
Edison Electric Institute
The Fertilizer Institute
Fort Howard Paper Company
Georgia Power Company
Gulf Power Company
Interstate Commerce Commission
Louisiana Power & Light Company
Middle South Utilities System
Mississippi Power & Light Company
Mississippi Power Company
Nevada Power Company
New Orleans Power Service, Inc.
Potomac Electric Power Company
Public Service Company of Indiana, Inc.
South Carolina Electric & Gas Company
South Carolina Public Service Authority
Southern Company Services, Inc.
The National Industrial Traffic League
United States of America
Virginia Electric and Power Co.
Western Coal Traffic League
Wisconsin Electric Power Company

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PETITION FOR WRIT OF CERTIORARI

Petitioners Commonwealth Edison Company, Madison Gas and Electric Company, Pennsylvania Power & Light Company, Wisconsin Power & Light Company and Wisconsin Public Service Corporation respectfully pray that a writ of certiorari issue to review the Judgment and Opinion of the United States Court of Appeals for the District of Columbia Circuit in this case.

OPINIONS BELOW

The decision of the Court of Appeals is reported as *Western Coal Traffic League* v. *United States*, 677 F.2d 915 (D.C. Cir. 1982) and appears as Appendix A to this Petition (Pet. App. A). The decision of the Interstate Commerce Commission which the Court of Appeals affirmed is reported at 364 I.C.C. 841 (1981) and appears at Pet. App. C.

JURISDICTION

The decision of the Court of Appeals, which constitutes its judgment in this case, was entered May 4, 1982. A timely Petition for Rehearing was denied by order entered June 15, 1982, which appears at Pet. App. B. The Court has jurisdiction to review the decision below under 28 U.S.C. §1254(1).

STATUTORY PROVISIONS INVOLVED

The basic statutory provision involved is 49 U.S.C. §10707a(a) (b) which appears at Pet. App. D. Also included in Pet. App. D are the following statutory provisions which are relevant to the questions presented:

49 U.S.C. §10707a, (c), (d), (e), (f), (g), (h); and 49 U.S.C. §10709.

STATEMENT

The Staggers Rail Act of 1980, Pub. L. No. 96-448,94 Stat. 1895 (1980) (the Act or the Staggers Act) deprived the Interstate Commerce Commission (Commission) of jurisdiction to pass on the maximum reasonableness of most railroad rates. It established a threshold below which the Commission would have no jurisdiction and further provided that, even as to rates above the threshold, Commission jurisdiction would extend only to rates for transportation over which the carrier possessed market dominance, defined as "an absence of effective competition from other carriers or modes of transportation for the transportation to which a rate applies." 49 U.S.C. §10709(a). The threshold was fixed at 160 percent of variable cost for the 12 months ending September 30, 1981, increasing 5 percentage points each 12 months thereafter until the "cost recovery percentage" takes over on October 1, 1983 or October 1, 1984.[1]

[1]For the 12 months begining October 1, 1983, the threshold is 175 percent of variable cost or the cost recovery percentage, whichever is less. For subsequent periods, the threshold is the cost recovery percentage but not less than 170 nor more than 180 percent of variable cost.

The Staggers Act establishes the rate in effect on October 1, 1980 as the base rate for an initial two year period.[2] The rates in effect on October 1, 1982, on October 1, 1984, and on October 1 of every fifth year thereafter become new base rates.

Section 203 of the Staggers Act contains two provisions authorizing increases in those base rates over which the Commission has jurisdiction. The Act directs the Commission to publish at least quarterly:

> a rail cost adjustment factor which shall be a fraction, the numerator of which is the latest published Index of Railroad Costs (which index shall be compiled or verified by the Commission, with appropriate adjustments to reflect the changing composition of railroad costs, including the quality and mix of material and labor), and the denominator of which is the same index for the fourth quarter of 1980, or for the fourth quarter of 1982 or for the fourth quarter of every fifth year thereafter, as appropriate. (49 U.S.C. § 10707a(a)(2)(B), Pet. App. D at 2))

Railroads have an absolute right to increase rates by the rail cost adjustment factor, and such increases cannot be challenged. (49 U.S.C. § 10707a(a)(b)(2), Pet. App. D at 2.)

In addition to the increases resulting from application of the rail cost adjustment factor, a railroad can increase rates, during the first 48 months after the October 1, 1980 effective date of the Staggers Act, by 6 percent in each 12 month period but not more than a total of 18 percent; and a railroad that has not achieved "revenue adequacy" as determined by the Commission can increase rates by 4 percent in each 12 month period thereafter. Such increases

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[2]Under Section 229 of the Staggers Act (49 U.S.C. §10709(d)(5)(B)), the base rate could be challenged within 180 days of the effective date of the Act but not thereafter.

may be challenged by complaint with the burden of proof on the shipper (49 U.S.C. §10707a(c) (d) (e); Pet. App. D at 2).

The initial draft of 49 U.S.C. §10707a(2) (B) had directed the Commission to use an "Index of Railroad Material Prices and Wages", which is the title of the index put out by the Association of American Railroads (the AAR Index). There was substantial shipper opposition to this provision, witnesses pointing out that the AAR Index made no adjustment for changes in productivity and overstated increases in cost. The language above quoted i.e., "with appropriate adjustments to reflect the changing composition of railroad costs, including the quality and mix of material and labor" was substituted by the Congress in response to such representations.

The AAR Index is an "input" index of the prices paid by railroads for wages and materials,[3] and not an "output" index of the railroads' costs of operation. In its decision in the rulemaking proceeding below, the Commission conceded that "productivity increases cause the costs of outputs to rise less rapidly than the costs of inputs...." (Pet. App. C at 6). It also conceded that "methodological problems of productivity measurement alone (although grave) do not preclude the development of productivity measures." (Pet. App. C at 6.) It continued, "We nevertheless question the reliability of such measures and as a matter of policy do not believe that their use is justified." (Pet. App. C at 6.)

After discussing its policy reasons, the Commission stated "In sum we will not adjust the rail cost index to reflect productivity gains as long as the railroad industry continues to earn inadequate revenues." (Pet. App. C. at 7.)

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[3]The existing AAR Index covers only 72 percent of price inputs. As a temporary surrogate for the 28 percent not covered by the AAR Index, the Commission decided to use the Producer Price Index. This temporary expedient is not involved in the questions here presented.

The Court of Appeals found the Commission decision "only minimally adequate." (Pet. App. A at 28.) It analyzed the policy reasons on which the Commission relied and rejected all of them. Nevertheless, although the Commission had conceded the feasibility of productivity adjustments and had rejected them solely on policy grounds, the Court of Appeals stated:

> We conclude that within the present state of the art—at least as reflected in this record—the difficulties of accurately measuring productivity growth on a current basis, coupled with the Commission's assessment of the importance of assuring railroads unencumbered rate increases to cover increased costs, support the Commission's conclusion that a productivity adjustment is inappropriate under present circumstances. (Pet. App. A at 35-36.)

In the face of the Commission's statement that it would not consider productivity gains so long as the railroad industry was earning inadequate revenues,[4] the Court continued:

> We expect, however, that in accordance with its stated intentions, the Commission will continuously review the accuracy of its chosen index and will revise the index in an appropriate fashion, including consideration of measurable productivity gains, as the circumstances warrant. (Pet. App. A at 36.)

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[4]This statement must be read in connection with the Commission's decision in Ex Parte No. 393, *Standards for Railroad Revenue Adequacy*, 364 I.C.C. 803 (1981), in which the Commission established standards of revenue adequacy that very few corporations could meet. Even the most prosperous of the nation's major railroads were found not to be revenue adequate. That decision is under review in *Bessemer & Lake Erie R.R.* v. *ICC*, No. 81-1492, *et al.* (3rd Cir. filed March 31, 1981).

REASONS FOR GRANTING THE WRIT

The Court below affirmed a Commission decision that squarely violates the statute by establishing rail cost adjustment factors that exceed increases in cost, and that will raise effectively and continuously the revenue/variable cost thresholds established by 49 U.S.C. §10709 (a) (2), which must be equaled or exceeded before the Commission can exercise jurisdiction over the maximum level of rates. The emasculation of the jurisdictional thereshold provision will permit monopolistic exploitation of shippers of commodities that are captive to the railroads and will cause incalculable harm to the nation's electric utilities and the customers they serve.

1. The sole purpose of the rail cost adjustment factor is to enable railroads to recover without delay increases in cost resulting from inflation. Other provisions of the statute provide ample authority to increase rates for other purposes (49 U.S.C. §10707a (c), (d)).[5] The legislative history makes this clear and the Court below so understood. The Court pointed out that in all the testimony at the Senate Hearings

> no one suggested that the function of the inflationary cost index was anything other than to provide a rapid mechanism for translating cost increases into rate increases. This view of the underlying purpose of the inflation index was reaffirmed when S. 1946 was reported out of committee. (Pet. App. A at 24.)

The Court further said that "we agree with petitioners that the *purpose* of section 203 was to allow railroads to keep up with cost increases . . . ." (Emphasis in original, Pet. App. A at 25.) So far, so good, but the Court went on to

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[5]The provisions authorizing rate increases are relevant only as to the relatively small amount of traffic over which the railroads possess market dominance. Rates on competitive traffic can be raised at will. See *supra*, p. 2.

interpret the statute as permitting the Commission to adopt knowingly and deliberately an index that greatly overstates increases in costs.[6]

In support of this misinterpretation of the statute, the Court stated that a secondary Congressional purpose was establishment of a cost recovery mechanism that would "avoid regulatory lag by operating with dispatch to assure that rates actually reflect current costs" (Pet. App. A at 23.) However, the Congressional objective of avoiding regulatory lag was to be accomplished by means of the requirement that the cost adjustment factors be published "as often as practicable but, in any event, no less than quarterly" (49 U.S.C. §10707a(a) (2) (B)). The objective of compensating the railroads for their increases in costs was to be accomplished by a cost adjustment factor that would compensate for increases in cost but *only* for increases in cost. The Court below confused the two objectives of "operating with dispatch" and "assur[ing] that rates actually reflect current costs." The Commission did not, and could not consistent with the statute, justify the use of an index which overstates costs on the ground that its use would prevent regulatory lag.

2. The Commission conceded that the development of productivity measures was feasible but rejected their adoption for policy reasons. The Court below carefully

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[6]The uncontradicted evidence in the record is that the overstatement of cost is substantial. For the years 1970 to 1978, the average annual increase in freight unit costs was only 66 percent of the increase in the AAR Index. (J.A. 816.) For the same 9 years, the average annual increases in the Consumer Price Index, the Producer Price Index and the GNP Implicit Price Deflator were, respectively, 63 percent, 79 percent and 62 percent of the average increase in the AAR Index. (J.A. 818.) The Western railroads have conceded that the AAR Index overstates railroad costs by 25% by basing escalation agreements on 80% of the Index. Staggers Rail Act of 1980: Hearings on S. 1946 before the Senate Comm. on Commerce, Science, and Transportation, 96th Cong., 1st Sess. (1979) at 435.

analyzed the policy reasons given by the Commission and rejected all of them (Pet. App. A at A-31-35). It then affirmed the Commission on the basis of its own views as to the difficulties of accurately measuring changes in productivity. In so doing, the Court erred in two respects. It invaded the primary jurisdiction of the Commission by substituting its judgment for that of the Commission on a factual issue, *See Atchison T. & S. F. Ry. Co.* v. *Wichita Board of Trade,* 412 U.S. 800 (1973), and it sustained the Commission order on a ground on which the Commission had not relied. *See SEC* v. *Chenery Corporation,* 317 U.S. 80 (1943).

3. The Court below seems to have construed the Commission's decision as an interim decision to be judged by the less stringent standards that apply to such decisions. Despite the Commission's statement that "we will not adjust the rail cost index to reflect productivity gains so long as the railroad industry continues to earn inadequate revenues," the Court below construed the decision as containing a commitment "to review the index against current cost data, taking appropriate action in the event of over recovery" (Pet. App. A at 31). We are unable to find such a commitment in the decision. The Commission said it would check for errors,audit underlying data and compare the AAR Index with other data sources (Pet. App. C at 3) but this is a far cry from a commitment to determine whether the AAR Index overstates cost increases and to take action in the event of over recovery.[7]

If an agency decision is erroneous, as was the Commission decision here, a court has a duty to remand the

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[7]There are methods of determining after-the-fact whether an index has overstated or understated increases in cost. One method would be to take a random sample of railroad traffic, cost it out on an annual basis and compare the increase in cost over the last 12 months with the increase produced by applying the rail cost adjustment factor. The Court did not require the Commission to make such a determination and the Commission does not propose to do so.

decision to the agency for correction. As stated in *FPC* v. *Idaho Power Co.*, 344 U.S. 17, 20 (1952): "the guiding principle . . . is that the function of the reviewing court ends when an error is laid bare. At that point, the matter once more goes to the Commission for reconsideration." An affirmance with simply precatory language leaves the agency free to correct its error or not as it sees fit.[8]

4. This case is of supreme importance to shippers of the few, but important, commodities that are captive to the railroads. The electric utility industry consumes a large portion of the coal mined in the United States and much of that coal is shipped for long distances over the railroads. There is no alternative to rail transportation for most movements of coal. Unless subjected to statutory or regulatory constraint, the railroads are free to price such traffic at monopoly levels. In enacting the Staggers Act, Congress sought to reconcile the need of the railroads for freedom in competitive markets with the need of captive shippers to be protected from monopolistic exploitation. One important place where this compromise is reflected is in the Jurisdictional threshold (49 U.S.C. §10709(d) (2)), which permits the railroads to charge rates much higher than they charge on competitive traffic but puts a limit on the extent to which they can engage in monopoly pricing without encountering regulatory control.

The effect of a rail cost adjustment factor that overstates increases in cost is to increase the effective threshold of

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[8]In an apparent response to the precatory language of the Court below, the Commission issued an Advance Notice of Proposed Rulemaking on July 23, 1982 which requested comments on "the possible use of the productivity adjustment in determining the quarterly rail cost adjustment factor and proposals for measuring productivity and for implementing a productivity adjustment." (Pet. App. E at 3.) This advance notice gives the shippers no assurance that a rulemaking proceeding will even be instituted. It certainly gives them assurance that a productivity adjustment will ever be adopted or when such an adjustment will be adopted.

Commision jurisdiction and to write out of the Act the protection against excessive monopoly exploitation that Congress thought it was giving to captive shippers.

Over time, a cost adjustment factor that is greater than the increase in railroad costs will insulate from regulation rates far in excess of the statutory jurisdictional threshold because neither the base rate nor a cost adjustment factor increase can ever be challenged by a shipper. This can be demonstrated readily. Assume that the threshold of Commission jurisdiction will be a revenue/variable cost ratio of 180% when the cost recovery percentage becomes the threshold,[9] and that the rail cost adjustment factor is derived from the AAR Index. Assume further that a rate that year is $1.80, that the variable cost of the service is $1.00, and that in the next year the AAR Index increases by 10% but the railroad's actual costs increase only 8%[10] The rate would thus become $1.98 ($1.80 x 1.10) but the variable cost would have risen only to $1.08 ($1.00 x 1.08). The revenue/variable cost ratio,and therefore the effective jurisdictional threshold, would become 183.3% ($1.98 divided by $1.08). In succeeding years, if the same situation continued each year, the increases in the effective threshold would be as shown below:

	Cost	*Rate*	*Effective Threshold*
Base Year	$1.00	$1.80	180%
Year 1	$1.08	$1.98	183.3%
Year 2	$1.166	$2.18	187%
Year 3	$1.259	$2.40	190.6%
Year 4	$1.36	$2.64	194.1%
Year 5	$1.469	$2.90	197.4%
Year 10	$2.158	$4.68	216.9%

[9]Beginning October 1, 1984, the cost recovery percentage will be the jurisdictional threshold only if it falls between 170 and 180 percent of variable cost. If it is less than 170 the threshold is 170 and if it is more than 180 the threshold is 180. 49 U.S.C. §10709(d)(2). The cost recovery percentage was found to be 197.5% of variable cost in 1981. 46 Fed. Reg. 20,794, 20,795 (Apr. 7, 1981).

[10]These assumptions are reasonable. See footnote 6, *supra* at 7 n. 6.

Under this scenario, the effective threshold of Commission jurisdiction would rise to a revenue/variable cost ratio of 216.9% at the end of just ten years and would continue to rise each year thereafter. The practical effect is that, over a ten year period, the railroad, without subjecting the rate to Commission jurisdiction, could raise the $1.80 rate to $4.67 per ton whereas it could have raised the rate only to $3.89[11] if the rail cost adjustment factor reflected actual increases in cost. If the increases in the AAR Index and in actual railroad costs are as assumed above, the impact on the consumers of electricity will be substantial. Since current rates on western coal typically exceed $20 per ton, a utility with annual requirements of 10 million tons of western coal will be faced with unjustified cost increases in year 10 in the order of 100 million dollars.

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[11]$1.80 compounded for 10 years at a rate of 8% is $3.89.

CONCLUSION

The Court below declined to set aside a Commission decision that it recognized was seriously flawed and that, if permitted to stand, will effectively write out of the Interstate Commerce Act what little protection the Staggers Act affords to captive shippers. In terms of its effect on shippers, this may well be the most important transportation case this Court has ever been asked to review.

For the reasons stated, certiorari should be granted and the case should be set for briefing and oral argument.

Respectfully submitted,

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